

**WRITTEN TESTIMONY OF  
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BEFORE  
HOUSE COMMITTEE ON GOVERNMENT REFORM'S  
SUBCOMMITTEE ON REGULATORY AFFAIRS  
ON  
IS THE FEDERAL GOVERNMENT DOING ALL IT CAN TO STEM  
THE TIDE OF ILLEGAL IMMIGRATION  
JULY 25, 2006**

**Introduction**

Madam Chairwoman Miller, Ranking Member Lynch, and Members of the Subcommittee, thank you for the opportunity to appear before you this morning.

I understand the focus of today's hearing is whether the Federal Government is doing all it can to stem the tide of illegal employment of aliens. I am pleased to discuss the IRS' limited role in this area.

**Framing the Issues**

Perhaps the most difficult part of these issues is framing them properly and understanding fully the different, yet sometimes complementary, roles performed by the Social Security Administration (SSA), the U.S. Department of Homeland Security (DHS), and the Internal Revenue Service (IRS).

We at the IRS support and appreciate the jobs being done at SSA in maintaining and protecting the Social Security Trust Funds and at DHS in enforcing our immigration laws, but our function is tax administration. Our job is to make sure that everyone who earns income within our borders pays the proper amount of taxes, even if they may not be working here legally. If someone is working without authorization in this country, he/she is not absolved of tax liability. Instead of an SSN to file a tax return, that person frequently uses an Individual Taxpayer Identification Number (ITIN).

An ITIN is a tax processing number issued by the IRS. It is a nine-digit number that always begins with the number 9 and has a 7 or 8 in the fourth digit, example 9XX-7X-XXXX.

IRS issues ITINs to individuals who are required to have a U.S. taxpayer identification number but who do not have, and are not eligible for a Social Security Number (SSN).

ITINs are issued regardless of immigration status because both resident and nonresident aliens may have U.S. tax return and payment responsibilities under the Internal Revenue Code. For example, a non-resident alien may have U.S. source income that is subject to U.S. tax. This often occurs in accordance with the provisions of a Tax Treaty.

It is important to understand that strictly from the standpoint of tax administration, the ITIN program is bringing taxpayers into the system. Thus far in calendar year 2006, we have received 1.6 million applications for ITINs, up 25 percent from this time last year.

We estimate that for tax periods 1996 to 2003 that the tax liability for ITIN filers totaled almost \$50 billion.

Comprehensive immigration reform --- including enhanced border security, robust interior enforcement, and a temporary worker program --- is a top Administration priority. The Administration believes that worksite enforcement is critical to the success of immigration reform. Further, as immigration laws are enforced, the Administration believes that comprehensive immigration reform also requires us to improve those laws by creating a temporary worker program that rejects amnesty and relieves pressure on the border. We also recognize the positive benefits for tax administration. For example, the creation of a temporary worker program will likely result in additional taxpayers entering the system.

### **IRS's Role in the Mismatch Program**

Each year, employers send their W-2s and W-3s to the SSA by February 28 (or March 31 if filed electronically). The SSA processes the forms and then attempts to reconcile any mismatches. They then send the information to IRS on a weekly basis. IRS culls out any unusable records, as well as any W-2s that are not related to the current tax year. For Tax Year (TY) 2004, the resulting IRS file contained more than 231 million W-2s from the SSA. This represents a decline of approximately 6.5 percent from the corresponding file for TY 2000.

Of the 231 million W-2s in IRS's TY 2004 file, approximately 223 million had matching names and SSNs. Some of these matches resulted from the SSA's successful use of techniques for resolving mismatches. For the balance of approximately 8 million TY 2004 W-2s for which there was no valid match, IRS used several additional methods to match the numbers. We were able to match approximately 60,000 more names with SSNs, about 7.9 million W-2s where there is no valid name and SSN match.

To help correct SSN mismatches, the SSA sends letters to employers, employees and self employed individuals asking that they take steps to match the names with the SSNs. These letters do not go to all employers. These letters go only to certain employers. First, letters are sent to employers who submit a wage report containing more than 10 Forms W-2 that SSA cannot process. In addition, employers who file more than 2200 W-2's, more than one-half of one percent (1/2 percent) of which represents mismatched forms, also receive the letters. In TY 03, the SSA sent over 121,000 such letters to

employers, inquiring about 7.2 million invalid W-2s. No letter was sent to the employers of the other 0.7 million mismatches

There are two interesting aspects to the data on mismatches. The first is geographical. Over 50 percent of the mismatches are found in four states, California, Texas, Florida and Illinois. California has the far greatest number of mismatches totaling nearly 2.3 million, or approximately 29 percent of the mismatch total.

The second is economic. Based on IRS' own analysis, about 75 percent of all mismatched W-2s report wages of less than \$10,000. If we focus only on those mismatched W-2s with no withholding, the percentage increases to 90 percent. Only about 2 percent of all W-2s with invalid SSNs report wages greater than \$30,000. In fact, the average wage for all mismatches is only about \$6700 annually. Bear in mind, that many employees receive more than one W-2 in a tax year, so these numbers may not reflect an individual's gross income.

From a tax administration perspective, we know that for TY 2004 there were approximately \$53 billion in wages reported on W-2s with invalid Social Security Numbers, with about a quarter of that amount, or \$13.3 billion, on W-2s with no withholding. About 56 percent of the \$53 billion came from W-2s reporting wages between \$10,000 and \$30,000.

On the high end, only about 1 percent of the wages (\$0.5B) were reported on mismatched W-2s showing wages in excess of \$100,000. Thus, we can conclude that W-2 mismatches represent the lowest wage earners who probably have little or no tax liability.

### **Legal Requirements for Employers**

It is important to point out that the SSA has no enforcement power and cannot impose penalties on employers for failure to correct SSN mismatches. IRS, however, does have enforcement power and can assess penalties. Therefore, it might be helpful if I walk you through our current legal authority.

Under section 6041 and 6011 of the Internal Revenue Code (IRC) employers and other payors must include correct SSNs or Taxpayer Identification Numbers (TINs) on Forms W-2 reporting wages or salaries paid to employees.

Under section 6721, we may impose a \$50 penalty on an employer for each W-2 or 1099 that omits or includes an inaccurate SSN/TIN unless the filer (employer, other payor, etc.) shows reasonable cause for the omission or inaccuracy. The maximum penalty for any employer or payor in a calendar year is \$250,000. If the violation is deemed to be willful, the fine is the greater of \$100 or 10 percent of the unreported amount per violation with no maximum.

From a tax compliance perspective, violations of these provisions are generally identified as part of an overall employment tax examination. We would not ordinarily initiate an

examination against an employer solely on the basis that he/she had reported a high number of mismatches. This is a function of both resources, and the fact that the employer can easily demonstrate that he/she has performed the due diligence required under the law.

Specifically, Section 6109 places the burden on the employee or the payee to provide the employer or payor with an accurate SSN or TIN. This is an important distinction because the employer can have any penalty imposed for failing to include an accurate SSN or TIN on the return abated, if the employer made an initial and, if necessary, annual request that the payee provide an accurate SSN/TIN. He can also have the penalty abated if he establishes that due diligence was otherwise used, such as by obtaining a statement from the employee under penalties of perjury that the SSN or TIN is accurate.

As you can see, what is important here is that the employer or payor makes a request, or repeats a request, for an accurate SSN or TIN. If the employer does, he/she has performed due diligence and has reasonable cause to believe the SSN or TIN is correct. Because this due diligence standard is so easy for employers to meet, it has been virtually impossible to sustain, under section 6724, a penalty assessed against an employer under section 6721.

## **Conclusions**

We continue to consider ways to improve the current system and stand ready to work with our colleagues at SSA and DHS in any manner we can. In addition, we would, of course, work to execute any changes Congress determines to bring into effect. Comprehensive immigration reform can have positive affects on tax administration. For example, the creation of a temporary worker program will likely result in additional taxpayers entering the system.

We would, however, call two issues to your attention that could be problematic with certain changes in the current regime.

First, any significant change requiring improved information sharing between Federal agencies or between Federal agencies and employers must account for protections found in section 6103 of the Internal Revenue Code. This section protects taxpayers from having their tax return information shared with third parties.

Second, we must make sure that any change in the current system encourages the type of behavior that we desire from both employees and employers. Failure to enact comprehensive reform could have negative consequences for tax administration if procedures are imposed on employers and employees that have the effect of driving certain economic activities “underground”. At least now we are collecting some taxes in these areas and we are working to collect even more.

Thank you for inviting me to testify this morning. I will be happy to take any questions you may have.